



Overview

Public-Private Partnerships

May 6, 2015

What is a Public-Private Partnership (PPP)?

- ▶ A **long-term contractual arrangement** between a public agency and private entity to **share risks and rewards** of a public asset and service delivery, through which the project **leverages the private sector's skills and financing** and provides **enhanced value for money**.
 - ▶ **Long-term contract** – lease, concession or similar structure
 - ▶ **Shared risks** – substantial transfer of risk to private partner relating to construction and operations and/or maintenance, including life cycle work
 - ▶ **Shared rewards** – compensation to private sector typically structured as availability payments or revenue sharing; business model should align interests – private partner should maximize profit only by meeting public goals
 - ▶ **Private sector skills** – PPPs are performance-based arrangements that allow for substantial private sector involvement in determining the design and construction specifications and discretion over maintenance and life cycle work, which leads to opportunities for technical innovations and efficiencies
 - ▶ **Private financing** – private sector responsible for financing capital costs
 - ▶ **Enhanced value for money** – PPP structure typically is advised or permitted when elements discussed above offer substantial quantifiable benefits to public agency
- ▶ **PPP ≠ new revenue**
- ▶ **Ultimate goal is to deliver public projects efficiently**

Why PPP?

▶ On time and on budget

- ▶ Accelerate project delivery and schedule certainty – aggregated procurement, risk transfer and payment structures can reduce time required to procure PPPs and minimize construction delays
- ▶ Reduce cost overruns – PPPs are typically procured on a lump-sum, fixed-price basis (i.e., private sector assumes risk of cost increases, unless created by public owner)
- ▶ Greater public budget certainty throughout the life of the PPP contract

▶ Cost savings through private sector innovation and efficiencies

- ▶ Private sector can bring technical innovations and expertise that may result in substantial cost savings, if properly incentivized (e.g., long-term operations and maintenance (O&M) scope and performance standards incentive to optimize life cycle work through better, up-front design and construction)
- ▶ Consolidated contract and single point of contact lead to improved efficiencies in service delivery and project management

Why PPP?

▶ Targeted risk allocation to private sector

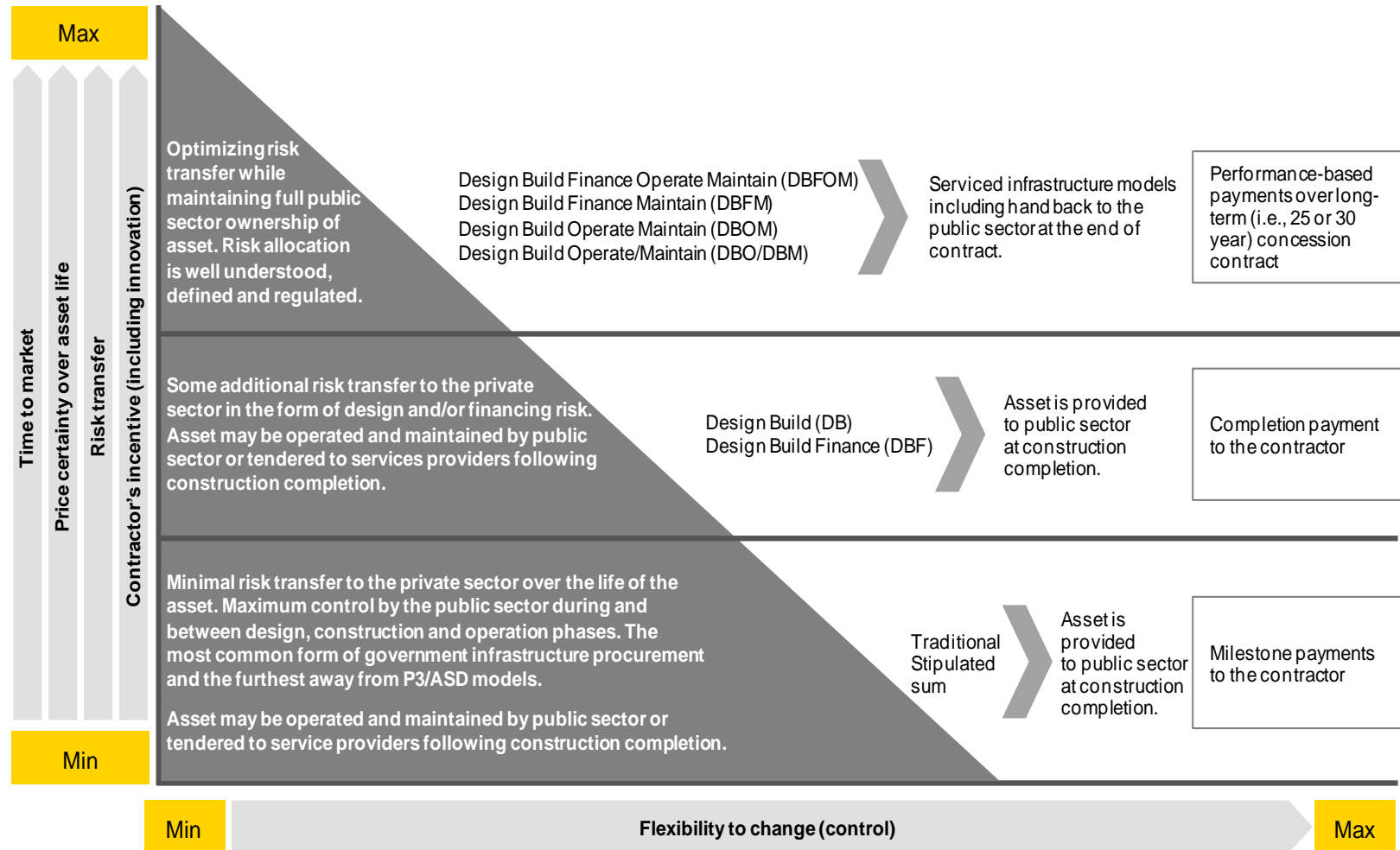
- ▶ Private sector better positioned to manage performance risks relating to design, construction, O&M and schedule (assuming public owner didn't initially overdesign the project)
- ▶ Public owner will achieve better value and cost-efficiency by retaining: (1) risks it is well positioned to manage (e.g., permitting, land acquisition, coordination with other public agencies) and (2) risks private sector cannot manage (e.g., force majeure, base interest rate fluctuation)

▶ Access to private capital

- ▶ Private sector provides up-front financing to deliver project and gets repaid with public funds and/or project revenues (e.g., user fees) during the operations and maintenance period of the asset
- ▶ Private sector has experience and flexibility in obtaining financing
- ▶ Private financing is critical for many public agencies that have limited capacity to issue debt and pay large sums of up-front capital costs for infrastructure projects
 - ▶ Characterization of developer financing relative to local borrowing constraints differs in each jurisdiction
 - ▶ Subject to appropriation obligations gaining acceptance in PPPs
 - ▶ Lower credit rating threshold for payments to developer creates opportunity to preserve ratings on direct debt obligations
- ▶ For transportation projects, private partner can access the lower cost tax-exempt market through Private Activity Bonds, and Treasury rate financing through the federal TIFIA loan program

Weighing PPP Options

A combination of approaches could be utilized to address different elements of the system plan



Growing U.S. Market for Availability-based Projects

- ▶ U.S. examples include:
 - ▶ Port of Miami Tunnel (closed)
 - ▶ I-595 Corridor Improvements and Express Lanes (closed)
 - ▶ **Denver RTD (closed)**
 - ▶ Long Beach Courthouse (closed)
 - ▶ Presidio Parkway (closed)
 - ▶ Goethals Bridge I-278 (closed)
 - ▶ Ohio River Bridges (closed)
 - ▶ Portsmouth Bypass (closed)
 - ▶ **Maryland Purple Line (in process)**
- ▶ Considerable interest for transit, high speed rail, as well as social infrastructure (courthouses, schools, etc)
- ▶ Being applied to HOT Lanes and toll facilities with toll revenues accruing to the public owner – e.g. I-595
- ▶ Hundreds of closed examples internationally (Canada, UK, etc)
 - ▶ UK PPP approach to transit disaggregates certain elements of a project

Availability Payments Summary

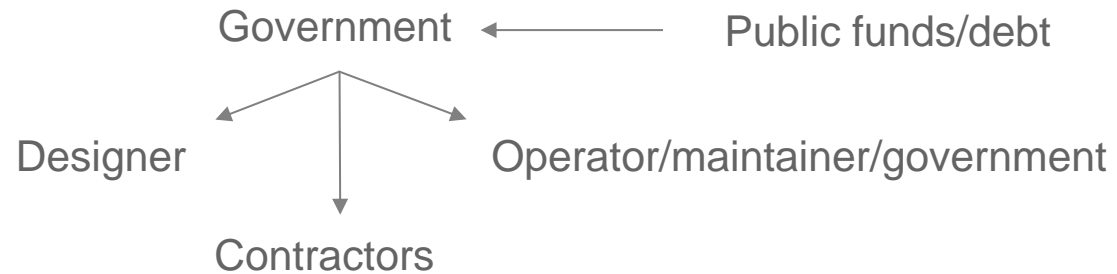
- ▶ Payments made to the Developer are earned:
 - ▶ Solely on the basis of meeting performance standards (regardless of user fees / market demand)
 - ▶ Payments are subject to deduction for failure to meet performance standards
 - ▶ Only after construction has been successfully completed (mitigating cost & delay risk)
- ▶ In return for the opportunity to earn payments:
 - ▶ Developer designs, builds, finances, operates and maintains facility for ~20-40 years
 - ▶ Equity investors and debt providers are at-risk if payments are not earned
- ▶ Generally appropriate for a project if:
 - ▶ It does not generate direct revenue or government wishes to retain control of rates
 - ▶ Revenue/demand is difficult to predict or influence
 - ▶ Service quality is more important or applicable goal than revenue maximization
 - ▶ Performance / operational outcomes can be defined and monitored
 - ▶ There are opportunities for innovative design solutions and/or lifecycle risk management
 - ▶ Strong public counterparty can credibly commit to make payments

PPP – More Than Just Financing

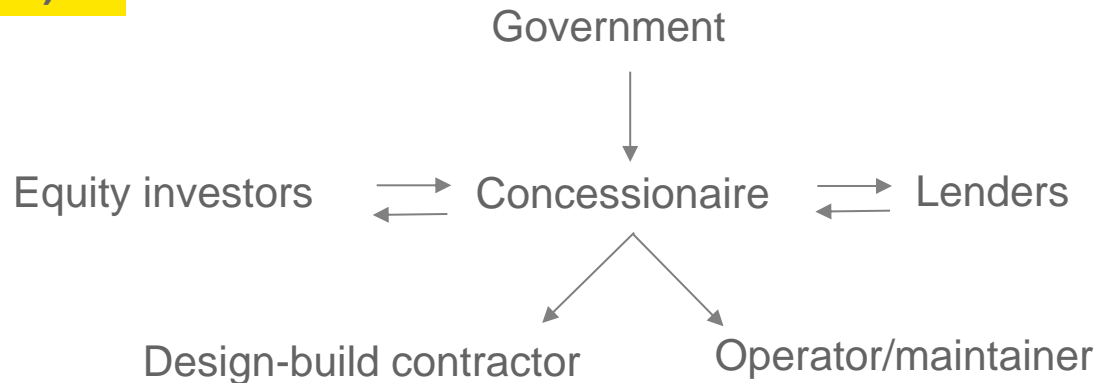
- ▶ Raising capital is not delivering a project and a traffic forecast is not the same as cash...
- ▶ Lifecycle of facility extends through and beyond duration of financing
- ▶ There can be significant sources of risk *besides demand*
 - ▶ How experienced is the owner in the delivery and O&M of a major project?
 - ▶ Who bears the risks of construction overruns, delays, operational underperformance, revenue shortfalls, higher than expected lifecycle costs, and/or unexpected or more frequent major maintenance?
 - ▶ Public trust is compromised if the performance and cost assumptions used to justify spending and dedicated taxes or other commitments are not achieved.
- ▶ Whether or not a PPP is ultimately warranted, considering a full range of delivery options fosters communication among disciplines and can lead to better outcomes and understanding of risks

Traditional vs. PPP Approaches – Contract Structure

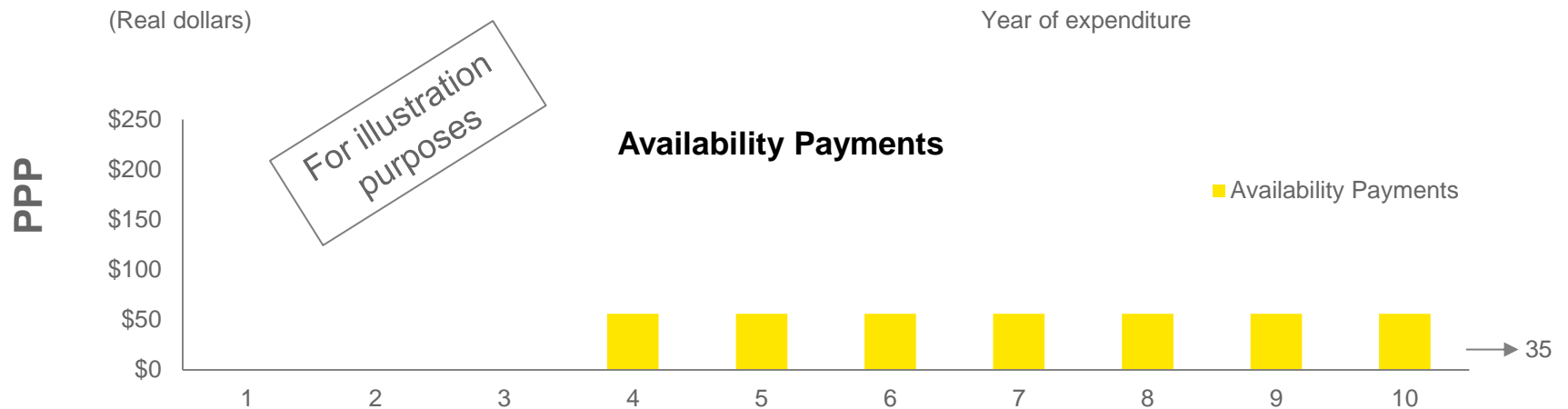
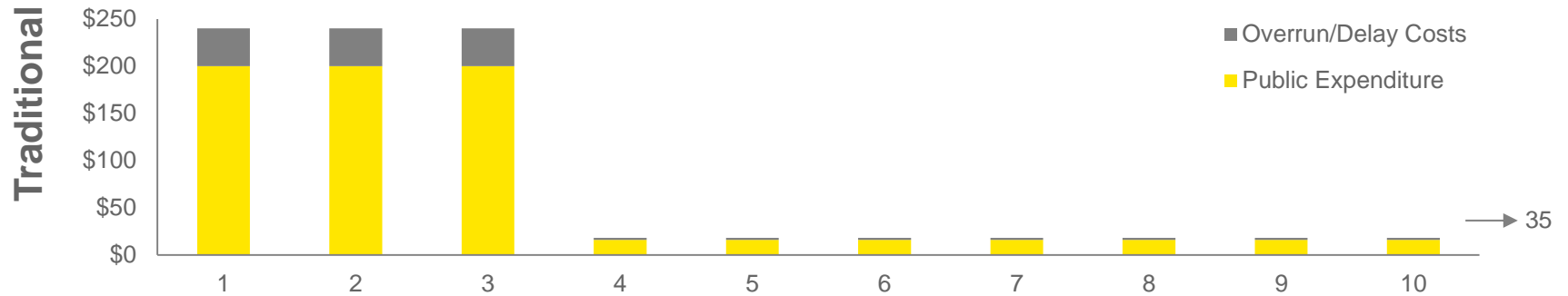
Traditional



PPP (DBFOM)



Traditional vs. PPP Approaches – Public Expenditures

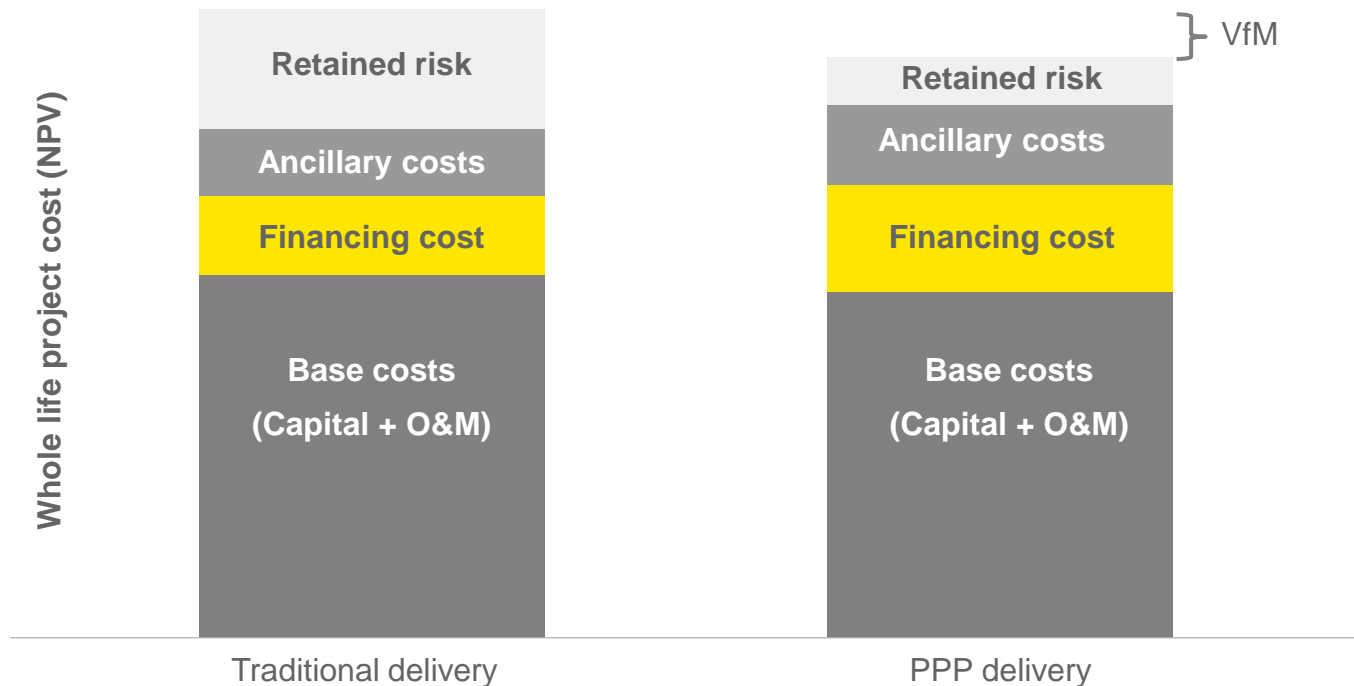


Note: these are very general approximations and conventional chart assumes major maintenance expenditures are smoothed as contributions to reserves.

Note: inherent warranty through de facto retainage.

Value for Money (VfM)

- ▶ Estimates the potential value of delivering a project under a PPP structure versus a traditional delivery approach
- ▶ PPP approach can provide cost savings if the potential savings on base costs and retained risks are greater than the higher ancillary and financing costs associated with private sector borrowing.
- ▶ Not all projects will allow for material innovation opportunities or transfer of risk to private sector at a reasonable cost.



Common PPP Challenges in the US

- ▶ Limited public sector experience with PPPs
- ▶ Higher transaction costs to develop and procure PPPs
- ▶ Understanding VfM and risk transfer
- ▶ Reduced flexibility to accommodate future demand and service delivery changes
- ▶ Complex to administer

Questions welcome

